STATE OF MICHIGAN

MICHIGAN SUPREME COURT

J & J FARMER LEASING, INC., FARMER BROTHERS TRUCKING CO., INC. CALVIN ORANGE RICKARD, JR., and JAMES W. RILEY, as Personal Representative of the ESTATE OF SHARYN ANN RILEY, Deceased,

Plaintiffs-Appellees,

v

CITIZENS INSURANCE COMPANY OF AMERICA,

Defendant-Appellant.
_____/

S. Ct. No. 125818
Court of Appeals No. 239069
L.C. No. 96-3742 NO

CITIZENS' SECOND SUPPLEMENTAL BRIEF IN SUPPORT OF APPLICATION FOR LEAVE TO APPEAL

PROOF OF SERVICE

PLUNKETT & COONEY, P.C.

BY: JEFFREY C. GERISH (P51338)
CHARLES W. BROWNING (P32978)
Attorneys for Defendant-Appellant
Citizens Insurance Co. of America
38505 Woodward Ave, Suite 2000
Bloomfield Hills, MI 48304
(248) 901-4000

TABLE OF CONTENTS

INDEX TO AUTHORITIES

CITIZENS' SECOND SUPPLEMENTAL BRIEF IN SUPPORT OF APPLICATION FOR LEAVE TO APPEAL

Citizens respectfully submits the following supplemental brief, which is intended to address two lines of questioning pursued by the Chief Justice and Justice Young at the March 8, 2005, oral argument on Citizens' application.

I. The Impact of *Theophelis v Lansing General Hospital*, 430 Mich 473; 424 NW2d 478 (1988) on Citizens' position in the instant case.

During the oral argument, Justice Young inquired about the impact of a case from this Court holding that, whereas a release and a covenant not to sue have the same effect as between the contracting parties, the impact as to third parties may be different. Undersigned counsel believes the case to which Justice Young was referring is *Theophelis v Lansing General Hospital*, 430 Mich 473; 424 NW2d 478 (1988).

In *Theophelis,* the Court recognized that, at common law, "a valid release of an agent for tortious conduct operates to bar recovery against the principal on a theory of vicarious liability, even though the release specifically reserves claims against the principal." 430 Mich at 480 (Opinion of Griffin, J.), and at 493 (opinion of Boyle, J.).[1] A covenant not to sue the agent, on the other hand, does not have the effect of releasing the principal. *Id.* at 492. See also, *Boucher v Thomsen,* 328 Mich 312; 43 NW2d 866 (1950); and *Cook v City Transport Corp,* 272 Mich 91; 261 NW 257 (1935). Citing secondary sources, the Court in *Theophelis* stated:

> The use and significance of a covenant not to sue has been explained as follows:
>
> > "A covenant not to sue is to be distinguished from a release in that it is not a present abandonment or relinquishment of

[1] The Court went on to hold that the common-law rule was not nullified by the Michigan Contribution Act, MCL 600.2925.

> the right or claim but is merely an agreement not to sue on an existing claim. It does not extinguish the cause of action. As between the parties to the agreement, the final result is the same in both cases. The difference is primarily in the effect as to third parties, and is based mainly on the fact that in the case of a release, there is an immediate release or discharge, whereas in the other case there is merely an agreement not to prosecute a suit."

Id. at 492, n14.

The reason a release of an agent has the effect of discharging the principal is "because release of the agent removes the only basis for imputing liability to the principal." *Id.* at 486. The reason a covenant not to sue does not remove the basis for imputing liability to the principal is that, unlike a release, it is not a relinquishment or discharge of a claim, but only a promise not to pursue it. In other words, a release is akin to saying that the agent did not commit a tort, whereas a covenant not to sue says only that the plaintiff will not pursue what may be a valid tort claim against the agent that continues to exist.

In the context of a bad-faith failure to settle claim, the insurer is not a joint tortfeasor, much less a joint tortfeasor whose liability is vicariously based on the liability of the insured tortfeasor. Unlike in the context of tort claims brought against a principal grounded in vicarious liability, in a failure to settle action against an insurer the release or relinquishment of a claim (or judgment) against the insured is not necessary to remove the basis of the insurer's liability. All that is necessary is that there not be a *collectable* judgment against the insured; if the judgment cannot be collected, an element of the failure to settle claim, namely damages, ceases to exist. *Frankenmuth v Keeley,* 433 Mich 525, 554; 447 NW2d 691 (J. Levin's opinion) ("There must be some showing that [the insured] has been damaged in order for there to be a recovery against an insurer for failure to settle" (citation omitted).) As established in *Keeley, collectability* from the

tortfeasors is the issue in the case against the insurer, not whether the tortfeasors were negligent, nor even whether a judgment against them exists.

Just as a release of an agent removes the only basis of liability on the part of the principal, the agreement in the instant case never to collect the judgment removes the only basis for finding liability against Citizens. The liability of Citizens requires as a precondition the existence of potential pecuniary loss to its insured. Because the promise to "forever forebear [sic: forbear] any action to collect any monies to satisfy the unpaid portion of the Judgment that the Plaintiff has against [the tortfeasors/insureds]" precludes collection of the unsatisfied judgment, the impact of the agreement as against Citizens is exactly the same as if the agreement had utilized language more in accordance with a conventional release. The rule discussed in *Theophelis, supra,* does not counsel otherwise.

II. Citizens' Proposed Mechanism For Proceeding With Bad Faith Failure to Settle Claims.

During the March 8, 2005, argument, a line of questions was asked, primarily by the Chief Justice, regarding Citizens' proposed mechanism of preserving bad faith failure to settle claims, what would be the practical implications of the Court adopting Citizens' position, and whether the Agreement at issue in the instant case is materially different than what was used in *Keeley*.

Citizens' position is that a proper understanding of the nature of a failure to settle action against an insurer requires as a prerequisite to the prosecution of such an action that the judgment against the insurer's insured (the tortfeasor) be actually collectable from the tortfeasor. So long as a claimant reserves the right to collect the judgment from the tortfeasor at some time in the future, the judgment remains actually collectable and the failure to settle claim is preserved.

Whereas actual collectability of the judgment is removed by an agreement to forever forbear any action to collect it, it is not removed by an agreement to decline temporarily to collect it.

The specific mechanism Citizens has proposed is for the claimant to agree not to take action to collect the judgment against the tortfeasor during the prosecution of a failure to settle claim against the insurer. The failure to settle claim can then either be assigned to the claimant or brought by the tortfeasor itself.[2] In the event the failure to settle claim is successful, the insurer will pay the damages, and the tortfeasor will be relieved of any obligation. If the failure to settle claim is unsuccessful, i.e., the insurer is found not to have failed to settle in bad faith, the claimant can then collect the judgment from the tortfeasor.

There is, of course, a critical difference as a practical matter between an agreement by the plaintiff never to collect a judgment from a tortfeasor on one hand, and an agreement not to collect the judgment unless and until a failure to settle claim against an insurer is concluded on the other.[3] Under the former arrangement, but not the latter, the judgment remains hanging over

---

[2] Plaintiffs' counsel's suggestion during oral argument that it was unclear at the time the Agreement was excecuted whether the Farmer entities could assign the failure to settle claim is belied by the fact that *Rutter v King*, 57 Mich App 152, 166; 226 NW2d 79 (1975), specifically held that such claims can be assigned by an insured to the claimant.

[3] The Court of Appeals reasoned that the language of the agreement used in *Keeley* is not relevant to this dispute because this Court's opinion in *Keeley* includes no analysis of the agreement used in that case. 260 Mich App at 620 n 8. To the extent the Court believes the Keeley agreement is relevant, Citizens notes that that agreement stated only that the plaintiff agreed "to forebear [sic: forbear] any action to collect monies to satisfy the Judgment he has obtained." (Plaintiff's Appendix, Exhibit B, p 4). The words "forbear" and "forbearance," without further qualification, imply a temporary refraining, as opposed to a permanent waiver, of the right to collect money. As one court put it:

> To forbear money is to refrain from collecting a debt. *See Boerner v. Colwell Co.*, 21 Cal.3d 37, 145 Cal.Rptr. 380, 384 n. 7, 577 P.2d 200, 204 n. 7 (1978) ("A 'forbearance' of money is the giving of further time for the repayment of an obligation or an agreement not to enforce a claim at its due date."); *H.V. Tygrett v.*

(Continued on next page.)

the tortfeasor's head, and the tortfeasor is subject ultimately to paying the judgment in the event of an unsuccessful failure to settle action.

Moreover, and perhaps more importantly, requiring the judgment to remain collectable in the event the bad faith failure to settle claim fails is the better rule because it will promote behavior and results that should be encouraged, and will also deter activity that should be deterred. The backdrop for any bad faith failure to settle claim against an insurer will be a judgment in excess of policy limits, and will involve two possibilities: either the judgment results from a damages assessment by a neutral fact finder, or it is a consent judgment. In both situations, public policy favors a rule requiring the over-limits judgment to remain ultimately collectable from the tortfeasor.

In the former scenario, it is assumed that the judgment accurately measures the claimant's damages, and, thus, it will always be the case that the tortfeasor insured has caused damages exceeding the limits of insurance coverage purchased by it. It is appropriate and consistent with

---

(Continued from previous page.)

> *University Gardens Homeowners' Ass'n,* 687 S.W.2d 481, 483 (Tex.App.1985) ("'Forbearance' occurs when there is a debt due or to become due, and the parties agree to extend the time of its payment.").

Berger v State Dept of Revenue, 910 P2d 581, 586 (Alaska, 1996). At a minimum, it is unclear whether the parties to the agreement in *Keeley* intended permanent or temporary refraining in utilizing the unqualified word "forbear." Citizens respectfully submits that they presumably intended temporary forbearance; else, why not just say that plaintiff agrees "not to collect", or "not to take any action to collect," rather than use the words "forbear" and "forbearance"?

In any event, the issue was not raised in that case. In the instant case, by significant contrast, the plaintiff and the insureds went out of their way to make sure there was no ambiguity, by changing the agreement to state that the plaintiff agreed to forbear "forever" from any action to collect any monies on the judgment.

public policy in that case for a collectable tortfeasor to remain exposed to potential collection in excess of policy limits. A tortfeasor that has caused over-limits damages ought to be subject to having to pay them, not only because it is fair in the abstract, but because that exposure will incentivize the tortfeasor to cooperate fully with its insurer in the defense of the action against the tortfeasor, and also to be active in pursuing settlement. If the tortfeasor is able to escape any exposure for the over-limits judgment caused by it, the tortfeasor is under no real incentive to do either, other than to do only what is necessary to comply with the terms of the insurance policy. Its primary incentive will be to bring about an arrangement with the plaintiff, either prior to or after trial, whereby it is released from any potential exposure to paying the over-limits damages that it caused.

Regardless of whether the failure to settle an action is caused by the insurer's bad faith, Citizens' proposed mechanism of requiring the tortfeasor to be potentially exposed to collection of the judgment pending the outcome of the bad faith claim would not unfairly impact the tortfeasor. If the failure to settle claim against the insurer is valid, the plaintiff can collect the excess judgment from the insurer and the tortfeasor will be under no further obligation. To the extent the tortfeasor suffers monetary damages as a result of having the judgment hanging over its head during the pendency of the failure to settle claim, it can collect those damages against the insurer as well. If the failure to settle claim against the insurer fails, then the tortfeasor, to the extent of its collectability, will be subject to collection of over-limits damages caused by it that it failed to avoid by itself settling the claim for a lesser amount—a result that is in no way unfair or undesirable.

This very case provides a good example of why Citizens' proposed mechanism is superior to a rule that allows a tortfeasor to bring (or assign) a failure to settle claim despite

having no exposure to paying the overlimits judgment. The Farmer entities, despite now conceding that they caused damage to the claimant greatly in excess of the limits of insurance purchased by them, were unwilling to contribute even $25,000.00 to resolve this case prior to trial. (See Citizens' Application, p 7). Presumably, had they known they would have to pay any over-limits judgment amount to the extent of their collectability unless it could be proven that Citizens failed in bad faith to settle the action, they would have been willing to remove such exposure for the relatively small amount of $25,000—especially given their claim in the instant action that they knew there was a genuine chance of a large verdict—and the underlying case would have settled to everyone's satisfaction long ago.[4]

With resect to the second scenario in failure to settle claims, where the judgment is entered with the tortfeasor's consent, Citizens' proposed mechanism would eliminate the incentive for collusion between the claimant and the tortfeasor that currently exists under the Court of Appeals' decision. To allow the tortfeasor (or the claimant via assignment) to pursue a failure to settle action against an insurer despite the existence of a covenant from the claimant never to collect the over-limits judgment is to encourage the tortfeasor to agree to judgment against itself in whatever amount necessary. As argued in Citizens' application, under the Court of Appeals' opinion, a tortfeasor would be wise to stipulate to any judgment amounts requested by plaintiff if, by doing so in exchange for the plaintiff's agreement never to collect, the

[4] Perhaps the Farmer entities would have refused to contribute $25,000 to settle the case even if they had known they could not avoid exposure to any over-limits judgment unless Citizens was proved to have committed bad faith. While Citizens respectfully submits that that is highly unlikely, the point is the same regardless. A tortfeasor faced with the decision whether to contribute to a settlement over limits ought to be making that decision with an understanding that it will be subject to collection of any judgment amount over limits unless it can be proven that the failure to settle was caused by the insurer's bad faith.

tortfeasor can avoid exposure to the over-limits amount. Such a rule encourages the creation of artificially high judgments that do not accurately measure damages, and encourages claimants and tortfeasors to collude to foist judgments in amounts exceeding policy limits on insurers. Citizens' proposed mechanism, on the other hand, would provide a disincentive to tortfeasors to engage in that type of collusion.

As for the appeal to tortfeasors of the temporary arrangement proposed by Citizens, it must be remembered that a tortfeasor that has become a debtor on a judgment exceeding policy limits is not in a position to insist on an agreement from the claimant never to collect the judgment—nor should it be in such a position. Absent collusion, such a state of affairs would exist only because the tortfeasor caused damages exceeding policy limits and the case did not settle for a lesser amount, either because the tortfeasor was unwilling to contribute enough money in excess of policy limits to settle the case, or because the insurer failed to settle the case in bad faith. In this scenario it would obviously behoove a collectable tortfeasor to accept a claimant's proposed agreement to hold off from collection efforts unless and until the bad faith failure to settle action is completed. If the failure to settle action succeeds, the tortfeasor will then be off the hook. If the failure to settle action fails, the tortfeasor will then be subject to collection of the judgment, but, again, there is nothing inappropriate about that result. The tortfeasor in this arrangement will also have an incentive to participate or cooperate with the claimant in prosecuting the failure to settle an action against the insurer.

The only tortfeasor that will be deterred from entering into the temporary agreement not to collect proposed by Citizens is the tortfeasor that is in a position to insist on permanent forbearance. And the only tortfeasor that would be in that position as a practical matter is one that has not, or probably has not, caused the claimant damages exceeding policy limits, but can

avoid any possible exposure by consenting to a judgment that purports to foist all damages on the insurer. To be sure, Citizens' proposed mechanism would presumably lead to a decrease in consent judgments of this type, but as noted above, such arrangements *should* be deterred.

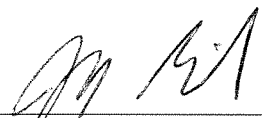
Finally, Citizens notes that the *amicus* briefs filed in this case unanimously support Citizens' proposed mechanism for proceeding with a failure to settle action as a practical, workable method. The Insurance Institute of Michigan, the American Insurance Association, the National Association of Mutual Insurance Companies, the Michigan Insurance Coalition, and the Michigan Defense Trial Counsel have all supported Citizens' position in this case. Indeed, the *amicus* brief filed by the American Insurance Association, the National Association of Mutual Insurance Companies and the Michigan Insurance Coalition argues specifically that Citizens' proposed mechanism of requiring that the judgment be collectable from the tortfeasor would be an appropriate and workable rule in this type of case. At the same time, not one person or group has filed an *amicus* brief suggesting Citizens' proposed mechanism would not work in practice or, if adopted, would lead to undesirable results.

RELIEF

For the reasons set forth above, in Citizens' Application for Leave to Appeal, in Citizens' Supplemental Brief, and by Citizens' counsel at oral argument, Citizens respectfully requests that this Court either (1) peremptorily reverse the Court of Appeals' opinion, and remand the matter to the trial court for entry of summary disposition in favor of Citizens; or (2) grant leave to appeal the complained-of opinion. Citizens further requests any and all relief to which it is entitled in equity and law.

Respectfully submitted,

PLUNKETT & COONEY, P.C.

By: 

JEFFREY C. GERISH (P51338)
CHARLES W. BROWNING (P32978)
Attorneys for Defendant-Appellant
38505 Woodward Ave, Suite 2000
Bloomfield Hills, MI 48304
(248) 901-4000

Dated: March 21, 2005

PLUNKETT & COONEY

Professional Corporation
Attorneys and Counsellors at Law

38505 Woodward Avenue
Suite 2000
Bloomfield Hills, MI 48304

(248) 901-4000
Fax (248) 901-4040
www.plunkettcooney.com

March 18, 2005

VIA FACSIMILE and U.S. MAIL
Robert E. Logeman, Esq.
2950 S. State Street
Suite 400
Ann Arbor, MI 48104

Re: J & J Farmer Leasing v Citizens Ins Co of America
Our File No. 00392.65111

Dear Mr. Logeman:

Please be advised that Citizens intends to file a second supplemental brief in this matter, designed to address certain questions asked during the oral argument on Citizens' application. I will send you a copy of the second supplemental brief and the motion for leave to file it by facsimile and regular mail as soon as the documents are filed. Citizens will not object should you wish to file a response to the second supplemental brief, or a supplemental brief of your own.

Sincerely,

Jeffrey C. Gerish
Direct Dial: (248) 901-4031
Email: jgerish@plunkettcooney.com

JCG/mmv

Blmfield.00392.65111.634683-1